Office Supreme Court, U.S.
FILED
JUN 18 1962
JOHN F. DAVIS, CLERK

In the

Supreme Court of the United States

OCTOBER TERM, 1961

No. 396

C. J. D. RUDOLPH AND IRMA M. RUDOLPH,
Petitioners,

v.

UNITED STATES OF AMERICA,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF OF PETITIONERS, C. J. D. RUDOLPH AND IRMA M. RUDOLPH

FELIX ATWOOD,
RICHARD A. FRELING, of
TURNER, WHITE, ATWOOD, MEER & FRANCIS,
1900 Mercantile Dallas Building,
Dallas 1, Texas,
Attorneys for Petitioners.

WARLICK LAW INC — 2263 VALDINA STREET — DALLAS — ME 1-3130

INDEX

	Page
OPINION BELOW	1
JURISDICTION	2
QUESTIONS PRESENTED	2
CONSTITUTIONAL PROVISIONS, STATUTES AND REGULATIONS INVOLVED	3
STATEMENT	3-10
Statement of Facts	3-9
Proceedings Before the Internal Revenue Service	9
Proceedings Before the Courts Below	10
SUMMARY OF ARGUMENT	11-15
ARGUMENT	15-45
I. PETITIONERS DID NOT CONSTRUCTIVELY RECEIVE INCOME WHERE THEY ATTENDED A BUSINESS CONVENTION AT THE BEHEST OF THE COMPANY, THE PAYMENT OF THEIR EXPENSES WAS NOT INTENDED AS COMPENSATION, AND THE CONVENTION WAS ORGANIZED AND EXPECTED TO SERVE THE LEGITIMATE BUSINESS PURPOSE OF INSTRUCTING AND MOTIVATING THE EMPLOYEES OF THE COMPANY	15-27
A. The Concept of a Non-Statutory Exception to Gross Income	15-19
B. The Concept Recognized in the Law	19-23
C. The Concept Applied to the Facts	23-27
II. IF THE PAYMENT OF EXPENSES ATTRIBUTABLE TO PETITIONERS' TRAVEL TO AND ATTENDANCE AT THE BUSINESS CONVENTION OF THE COMPANY CONSTITUTES TAXABLE INCOME TO PETITIONERS, THEN AN EQUIVALENT AMOUNT IS DEDUCTIBLE BY THEM AS AN ORDINARY AND NECESSARY BUSINESS EXPENSE	27-44

Page

A. Legislative History of the Statute . 28-31

B. Refinement of the Issues 31-36

C. Petitioners Attended the Convention for Business Reasons 36-44

1. There is no valid basis for distinguishing between travel time and the various activities of the convention as to their business purpose 39-41

2. Because Petitioners were compelled by the Company to attend the convention, all their actions (and the expenses incurred in connection therewith) were for a legitimate business purpose directly and proximately related to Rudolph's business 41-44

III. If the Petitioners Are Charged With Income in This Case, the Expenditures Attributable to Irma M. Rudolph, as Well as Those Attributable to Her Husband, Are Deductible as Ordinary and Necessary Business Expense 44-45

Conclusion 45

Appendix A 47

Appendix B 57

Page

Cases:

Benaglia, Arthur, 36 B.T.A. 838 (1937) 21

Bingham's Trust v. Comm'r, 325 U. S. 365, 65 S. Ct. 1232 (1945) 30

Bistline v. United States, 145 F. Supp. 802 (D. Idaho 1956) 33

Boykin v. Comm'r, 260 F. 2d 249 (8th Cir. 1958) 21

Bryers v. Comm'r, 199 F. 2d 273 (8th Cir. 1952) 33

Callinan, Rita N., 1953 P-H T.C.M., dec. 53,055 34

Canton Cotton Mills v. United States, 94 F. Supp. 561 (Ct. Cl. 1951) 32

Carton, Henry, 30 T.C. 28 (1958) 33

Caughlin v. Comm'r, 203 F. 2d 307 (2d Cir. 1953) 33

Comm'r v. Duberstein, 363 U. S. 278, 80 S. Ct. 1190 (1960) 23, 25

Comm'r v. Flowers, 326 U. S. 465, 90 L. Ed. 203, 66 S. Ct. 465 (1946) 31

Comm'r v. Glenshaw Glass Co., 348 U. S. 426, 99 L. Ed. 483, 75 S. Ct. 473 (1955) 16, 17

Comm'r v. Smith, 324 U. S. 177 (1945) 11, 16

Corliss v. Bowers, 281 U. S. 376 (1936) 21

Deputy v. DuPont, 308 U. S. 488, 60 S. Ct. 363 (1940) 32

Doffey, Robert C., 21 B.T.A. 1242 (1931) 34

Dowling, J. N., 4 B.T.A. 499 (1926) 34

Eisner v. Macomber, 252 U. S. 189, 64 L. Ed. 521, 40 S. Ct. 189 (1920) 16

Ellis, Wade, H., 15 B.T.A. 1075 (1929) 34

Farmers Loan & Trust Co. v. Minnesota, 280 U. S. 204, 74 L. Ed. 371, 50 S. Ct. 98 (1930) 11

	Page
Finkenburg's Sons, Inc. 17 T.C. 973 (1952)	34
General American Investors Co., Inc. v. Comm'r, 211 F. 2d 522 (2d Cir. 1954), *aff'd*, 348 U. S. 434, 99 L. Ed. 504, 75 S. Ct. 478 (1955)	17
Gunther, Charles O., Jr., 1954 P-H T.C.M., dec. 54,287	33
Jack, Cecil M., 13 B.T.A. 726 (1928)	34
James v. United States, 366 U. S. 213, 81 S. Ct. 1052 (1961)	16
Kornhauser v. United States, 276 U. S. 145 (1927)	30
Lilly v. Comm'r, 343 U. S. 90, 72 S. Ct. 497 (1952)	33
Merchant's Loan & Trust Co. v. Smietanka, 255 U. S. 509, 65 L. Ed. 751, 41 S. Ct. 386 (1921)	18
Noland v. Comm'r, 269 F. 2d 108 (4th Cir. 1959)	32
Old Colony Trust Co. v. Comm'r, 279 U. S. 716, 73 L. Ed. 918, 49 S. Ct. 499 (1929)	16
Pacific Grape Products Company, 17 T.C. 1097 (1952)	34
Patterson v. Thomas, 289 F. 2d 208 (5th Cir. 1961)	25, 35
L. F. Ratterman, 1948 P-H T.C. Memo, Dec. 48,130, *aff'd without opinion*, 177 F. 2d 204 (6th Cir. 1949)	34
Robinson Land & Lumber Company of Alabama v. United States, 112 F. Supp. 33 (S.D. Ala. 1953)	32
Shutter, Marion D., 2 B.T.A. 23 (1925)	33
Silverman, Alexander, 6 B.T.A. 1323 (1927)	34
Squier, J. Bentley, 13 B.T.A. 1283 (1928)	34
Summerour v. Allen, 99 F. Supp. 318 (M.D. Ga. 1951)	34
Tinkoff v. Comm'r, 120 F. 2d 564 (7th Cir. 1941)	32

	Page
Towne v. Eisner, 245 U. S. 418 (1918)	11
Upham, Ray, 16 B.T.A. 950 (1929)	34
Welch v. Helvering, 290 U. S. 111, 54 S. Ct. 8 (1933)	32
Williams, Clarence K., 35 T.C. , No. 74 (1961)	17
Wolfe v. Comm'r, 59-2 USTC 9558 (4th Cir. 1959)	21
Wolfe v. McCaughn, 17 AFTR 1007 (E.D. Pa. 1933)	34
Constitutional Provisions:	
Amendment XVI	3
Statutes:	
Internal Revenue Code of 1954, 26 U.S.C. § 1 et seq. (1958 Edition):	
Section 61	3
Section 62	3
Section 63(a)	3, 28
Section 119	19, 21
Section 161	3, 28
Section 162(a)	3, 28, 29, 31
Section 262	29
Section 7807	31
Internal Revenue Code of 1939, Sec. 22, 26 U.S.C. § 22 (1952 Edition)	16
Revenue Act of 1916, Sec. 5(a)	28
Revenue Act of 1917, Sec. 1201(1)	28
Revenue Act of 1918, Sec. 214(a) and 215(a)	28, 29
Revenue Act of 1921, Sec. 214(a)(2)	29

	Page
Revenue Act of 1928, Sec. 23(a)	29
Tariff Act of 1913, Sec. II,B	28
United States Treasury Regulations:	
Reg. 62, Art. 101(a)	31
Reg. 65, Art. 101	30
Reg. 69, Art. 101	30
Reg. 74, Art. 121	30
Reg. 77, Art. 121	30
Reg. 86, Art. 23(a)-1	30
Reg. 94, Art. 23(a)-1	30
Reg. 101, Art. 23(a)-1	30
Reg. 103, § 19.23(a)-1	30
Reg. 106, § 402.227	22
Reg. 107, § 403.227	22
Reg. 111, § 29.23(a)-1	30
Reg. 118, §§ 39.23(a)-1 and 39.23(a)-2(a)	3, 30, 31
Reg. § 1.119-1(c)(2)(1954)	21
Reg. §§ 1.162-2(b), (c), and (d)(1954)	3, 30, 31, 32, 36, 37, 44
Reg. § 1.162-5(1954)	35
Reg. § 1.162-17(b)(1954)	27
Reg. § 31.3401(a)-1(b)(10)(1954)	22
Revenue Rulings and Releases:	
I.T. 2602, 1931 Cum. Bull. 130	34
I.T. 3448, 1941-1 Cum. Bull. 206	34
I.T. 4012, 1950-1 Cum. Bull. 33	32
Mim. 6472, 1050-1 Cum. Bull. 15	20
Rev. Rul. 190, 1953-2 Cum. Bull. 302, 305	32
Rev. Rul. 58-240, 1958-1 Cum. Bull. 141	33

Page

Rev. Rul. 59-307, 1959-2 Cum. Bull. 48 21

Rev. Rul. 59-316, 1959-2 Cum. Bull. 57 35

Rev. Rul. 60-16, 1960-1 Cum. Bull. 58 32, 35

Rev. Rul. 60-348, 1960-2 Cum. Bull. 41 21

News Release, IR-394, August 3, 1961, 4 P-H Fed. Tax Serv., par. 32,375 (1961) 39

Texts:

Mertens, Law of Federal Income Taxation 20, 32, 33

Simons, Personal Income Taxation 53 (U. Chicago Press 1938) 18

Surrey & Warren, Federal Income Taxation Cases and Materials 106 (Foundation Press, Inc. 1955) 19

Miscellaneous:

105 *Congressional Record* 11897, 11900 30

H. R. No. 350, 67th Cong., 1st Sess. p. 11 (1921) 29

H. R. No. 2333, 77th Cong., 2d Sess., p. 75 (1942) 30

S. B. 2040, *to amend* H. R. No. 7523, 86th Cong. 29

Sen. Rep. No. 275, 67th Cong., 1st Sess., p. 14 (1921) 29

Sen Rep. No. 1622, 83d Cong., 2d Sess. pp. 168, 190 (1954) 16, 21

Caplin, *The Travel and Entertainment Expense Problem*, 39 Taxes 947 (December, 1961) 46

Life Magazine (September, 1952) 22

Report No. 15, Life Insurance Sales Research Bureau (November, 1924) 23, 35, 41

Tansill, Joseph E., 14 Journal of Taxation 201, 202 (1961) 45

The Royal Bank of Canada Monthly News Letter, Vol. 39, No. 2, p. 1 (February, 1958) 24

Wall Street Journal, September 29, 1961 42

In the

Supreme Court of the United States

OCTOBER TERM, 1961

No. 396

C. J. D. RUDOLPH AND IRMA M. RUDOLPH,
Petitioners,

v.

UNITED STATES OF AMERICA,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

---

BRIEF OF PETITIONERS, C. J. D. RUDOLPH AND IRMA M. RUDOLPH

OPINION BELOW

The majority and dissenting opinions of the Court of Appeals for the Fifth Circuit (R. 96-102) are reported at 291 F. 2d 841-845. The opinion and judgment of the Federal District Court for the Northern District of Texas, Dallas Division, was issued September 28, 1960 (R. 78-82), and is reported in 189 F. Supp. 2.

JURISDICTION

The judgment of the Court of Appeals was entered June 27, 1961 (R. 96). The petition for a Writ of Certiorari was filed on September 11, 1961. The Writ of Certiorari was granted November 13, 1961 (R. 106). The jurisdiction of this Court rests upon 28 U. S. C. 1254(1).

QUESTIONS PRESENTED

1. Whether an insurance agent realizes taxable income when the insurance company for which he works pays his and his wife's expenses of traveling to and attending a convention of the company's agents where, because of concern for his economic security, he is compelled by the company to attend, has no control over the mode of travel, accommodations or activities, and the convention is designed and intended primarily for the business purposes of the company not as compensation to the agent.

2. Whether, in the alternative, the reasonable expenses of an insurance agent in traveling to and attending a convention of agents of the insurance company for which he works constitute ordinary and necessary expenses of carrying on a trade or business where the business of the convention is directly related to his job and where, because of concern for his economic security, he is compelled by the company to attend.

3. Whether, in the alternative, the reasonable expenses of an agent in bringing his wife to a business convention under the foregoing circumstances constitute ordinary and neces-

sary expenses of carrying on a trade or business where, as part of a long-range and continuous program of business education, the company expects that the wife attend and would view with disfavor her failure to attend without adequate reason.

CONSTITUTIONAL PROVISIONS, STATUTES AND REGULATIONS INVOLVED

This case involves the Sixteenth Amendment to the Constitution of the United States; Sections 61, 62(1) and (2), 63(a), 161 and 162(a) of the Internal Revenue Code (1954) [26 U. S. C. §§61, 62(1) and (2), 63(a), 161 and 162(a)]; U. S. Treas. Reg. 118, §§ 39.23(a)-1 and 39.23(a)-2; and U. S. Treas. Reg., §§1.62-1(a) and (c)(1) and 1.162-2 (1954) [26 C. F. R. §§1.62-1(a) and (c)(1) and 1.162-2], pertinent provisions of which are printed in Appendix A, p. 47.

STATEMENT

Statement of Facts. The Southland Life Insurance Company (hereinafter sometimes referred to as "Company") sponsors a national convention for certain of its agents and their wives approximately every eighteen months (R. 31). The Company convention is traditional in the life insurance business (R. 65), having been recognized for at least thirty-five or forty years as one of the most effective types of sales procedure for training the agents and improving their morale (R. 68). It is one of the established roots of agency management (R. 69).

The management of the Company, especially Kenneth B. Skinner, the Vice President and Agency Director, and his staff worked for many months in arranging for the 1956 convention of the Company's agents in New York City (R. 45, 46). They put into effect a program designed to attract the agents and their wives, selected the means of transportation and chartered special trains to take the agents, their wives, and certain of the Company officials and their wives to the convention. They provided transportation from the train to the hotel which they had selected and arranged the rooms to be occupied, scheduled the time and context of the formal business program, arranged for various group activities for the persons attending the convention, and provided group transportation for most of the events and back to the special train for return to Dallas. All persons attending the convention were required to abide by transportation, accommodation and activity arrangements (R. 25, 28).

The Petitioner, C. J. D. Rudolph (hereinafter sometimes referred to as "Rudolph"), has continuously worked for the Company since September 14, 1932, as an ordinary life insurance agent (R. 22, 41). He was an independent contractor of the Company under a contract terminable at the will of the Company (R. 43).

The Company selects men to attend a convention based upon their proven abilities, as well as their aptitude for the insurance business; the amount of insurance written is an important yardstick in measuring their ability (R. 61).

The Petitioners were invited to the convention for the purpose of instruction (R. 49), and for the purpose of communicating to the agents the Company's objectives and plans (R. 46). Rudolph had written an amount of business during a specified period which made him and his wife eligible to be asked by the Company to attend the convention. The yardstick used by the Company for determining eligibility to attend the convention was not intended to single out certain men for a prize or award (R. 46); rather, the Company management concluded that these agents would be most likely to benefit from the overall program of the convention, including informal discussions among agents and the officers of the Company (R. 62). Even though an agent was eligible, he could not attend unless invited by the Company (R. 49).

The Company deems the conventions to be of such importance that it looks with serious displeasure upon any agent or his wife who, without good reason, does not attend (R. 54). The Company management considers it a part of the agent's duty and responsibility to attend a convention when invited (R. 61, 74). Rudolph believed that he and his wife were required to attend the convention (R. 28), and he did not feel that the convention trip was a vacation (R. 43, 45). The convention site was selected out of the rather limited number of cities available to meet the criteria of the Company, such as housing all of the group in one hotel, having facilities for meeting rooms, transportation and availability of speakers (R. 57, 58).

Petitioners, along with 293 Southland agents, officers and employees (R. 48), left Dallas, Texas, by special trains

about 9:30 P.M. on Tuesday, December 11, 1956, and arrived in New York City on the evening of Thursday, December 13, 1956 (Pl. Ex. 10, R. 83), about dark (R. 34).

The formal business session of the convention commenced at 9:30 A.M. on Friday, December 14, 1956, and the following is a summary of the agenda of such session (Pl. Ex. 11, R. 86, 87): Kenneth B. Skinner, Vice President and Agency Director, presided; the Invocation was given by Neil H. Wright, Lubbock, Texas; Ben H. Carpenter welcomed the conventioners to New York; there followed an agents' panel discussion with the theme "Success Through Planning" in which the Director of Sales Training and some of the leading agents of the Company participated; Glenn M. Brooks told of "The 1957 Agency Activity Program"; next was a speech by Dan C. Williams, President of the Company, on "Our Southland Life Future"; followed by an address by John W. Carpenter, Chairman of the Board, on the subject "Your Company and Mine." At 12:30 P.M. on that day the agents and officers of the Company attended a luncheon presided over by Field Scovell, Vice President and Superintendent of Ordinary Agencies, and the principal address was given by Dr. Norman Vincent Peale, whose subject was "Success Through Right Thinking." It was arranged that his address, while inspirational in character, would fit in with the theme of the convention (Pl. Ex. 14, R. 89, 90), and he accomplished such purpose (R. 52). On the afternoon of Friday, December 14th, following the luncheon, sightseeing buses took the agents and their wives on a sightseeing tour which ended about 5:30 P.M. (Pl. Ex. 10, R. 84).

On Saturday, December 15th, a breakfast and fashion show for ladies only was held but was not attended by Mrs. Rudolph (R. 38). Tickets were provided for a special Christmas show at Radio City Music Hall at 1:15 P.M. on Saturday, December 15, and at 6:30 P.M. buses were provided to transport the agents and their wives to the Copacabana for dinner, dancing and a floor show, with buses returning at 10:00 P.M. (Pl. Ex. 10, R. 84, 85). On Sunday morning, December 16th, buses were provided for the transportation of the Southland personnel attending the convention from the hotel to the trains (Pl. Ex. 10, R. 86), and the trains arrived in Dallas on December 18th.

All aspects of the convention were determined by the management of the Company, including the time and mode of travel, the place, location and character of the convention, the hotel accommodations, as well as all other activities of the convention (R. 32, 46). Neither the agent nor his wife did or could receive anything in lieu of going to the convention (R. 32, 54). The Company provided no liquor and held no cocktail parties (R. 43).

The Government does not question the bona fides of the convention (R. 67). The travel to and from the convention, as well as the various entertainment activities of the convention, were planned so that the agents and officers of the Company would be together in groups at all possible times, because it was the opinion of the Company management that the informal exchange of ideas among the agents and officers was of as great importance as the formal business sessions (R. 62) and furthered the essential business purpose

of the convention (R. 69, 74). The Petitioner, Rudolph, participated in these informal discussions not only in New York City, but on the train up and back (R. 29), and in his judgment the convention helped him in his business (R. 28).

The Company considers that an agent's wife plays an important role in his career (R. 52, 53), and her help may determine his success or failure (R. 46). The conventions sponsored by the Company are designed to furnish a program of instruction and association with the other wives of agents and Company officials which serves to teach an agent's wife how to help her husband (R. 53). Her presence serves a bona fide business purpose (R. 69), and is deemed desirable by the Company management (R. 48, 53). The wife's importance to her husband's business is recognized by the Company. The Company requires an interview with the wife in the agent's home prior to employment of the agent so that she may be fully aware of the contribution she can make to her husband's success (R. 53). The Company distributes a booklet to the wife of a new agent entitled "A New Partnership Has Been Formed", the purpose of which is to show her how she can help her husband in the life insurance business (R. 53). From time to time, letters are sent to the wife, and a monthly publication for the employees is mailed to the agents' home so that the wife will have a convenient opportunity to read it (R. 53). The Company has determined that the presence of wives at the conventions keeps the meeting pitched on a high and attentive level (R. 53). The Managing Director of the Life Insurance Agency Management Association

testified that it was a wise business practice to have an agent's wife at the convention and to indoctrinate her with her prospects and responsibilities of the wife of an insurance agent (R. 69, 70).

Proceedings Before the Internal Revenue Service. Petitioners timely filed their joint Federal Income Tax Return for the calendar year 1956 (R. 5, 19, 22), and timely paid the tax thereon (R. 5, 19). Subsequently thereto, the Commissioner of Internal Revenue assessed a deficiency in income tax for such year against Petitioners in the amount of $126.90.

The entire expense attributable to Petitioners' travel to and from and their attendance at the convention, with the exception of $30.00 given to Petitioners as an allowance for unplanned meals in New York City, was paid directly by the Company to third parties (R. 36). The $30.00 was spent for the purpose for which it was given (R. 26). The parties have agreed that the total amount of travel and convention expense allocated to Petitioners was approximately $560.00 (R. 51).

The deficiency assessed against Petitioners resulted from the Commissioner's including in their income the amount of expenditures made by the Company and allocated to them as stated above, and by the further action of the Commissioner in disallowing to Petitioners a business expense deduction for an amount equivalent of the income with which they were charged.

Petitioners paid the assessed deficiency in income tax on September 8, 1958, together with the interest thereon, and timely filed a claim for refund, which was denied (R. 5, 19).

Proceedings Before the Courts Below. Petitioners instituted suit against Respondent on October 9, 1959 (R. 24) in the Federal District Court for the Northern District of Texas to recover the $126.90 in income tax, together with interest thereon in the amount of $10.19, for the calendar year 1956, which taxes were alleged to be illegally and erroneously assessed against and collected from Petitioners by the District Director of Internal Revenue for the district in which Petitioners reside (R. 5, 19). The August 31, 1960 (R. 4). The cause came on to trial before Honorable T. Whitfield Davidson, sitting without a jury, who, on September 28, 1960, entered judgment for Respondent (R. 81).

Petitioners filed due notice of appeal to the United States Court of Appeals for the Fifth Circuit (R. 82), and on June 27, 1961, that Court affirmed the judgment of the Trial Court per curiam, Judge Brown dissenting (R. 92-102). Formal judgment was entered by said Court on June 27, 1961 (R. 103). Petitioners filed a motion for rehearing on July 18, 1961 (R. 103-104), and the order denying the motion for rehearing was entered by said Court on July 28, 1961, Judge Brown again dissenting (R. 105). Petitioners filed in this Court on September 11, 1961, a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit. This Court granted Certiorari on November 13, 1961 (R. 106).

SUMMARY OF ARGUMENT

I.

Justice Holmes, in *Towne v. Eisner*, *245 U. S. 418 (1918)*, remarked:

> "A word is not a crystal, transparent and unchanged; it is the skin of a living thought and may vary greatly in color and context according to the circumstances and the time in which it is used."

Once again the Court is called upon to construe the restless word "income"; to resolve whether or not, under the Sixteenth Amendment and the taxing statutes enacted pursuant thereto, Petitioners realized income with respect to expenditures, incurred by the Company in sponsoring a convention of its agents, of which a stipulated amount was allocable to Petitioners. The intensely practical matter of taxation[1] is here concerned with an intensely practical aspect of contemporary business life—the company convention—and all its overtones of economic compulsion, modern management practices, business psychology and the like. It is in this setting that the color and context of the word "income" is sought.

While it is recognized that the Court, in specific situations, has accorded broad meaning to the word "income",[2] there exists an area wherein an employee may be the recipient of or enjoy something which, from the standpoint of classical or philosophical economics or, perhaps, in a very real sense,

[1] Farmers Loan & Trust Co. v. Minnesota, 280 U. S. 204, 74 L. Ed. 371, 50 S. Ct. 98 (1930).

[2] Comm'r v. Smith, 324 U. S. 177 (1945).

represents a gain or benefit to the employee, but he is not considered to be in receipt of taxable income. A careful analysis of the decisions and the logic of the tax law suggests that this condition is present when (i) the employer does not intend the thing provided to be additional compensation to the employee; (ii) there is no undeniable accession to wealth, clearly realized, over which the employee has complete dominion; and (iii) the dominant motive of the employer is to further his business and the thing provided is designed to accomplish that end. In other words, the revenue laws do not purport to tax what is akin to psychic income or the perquisites of employment.

In the case before the Court, the Company sponsored and paid for a convention of its agents because, in the judgment of its management based upon long-standing personal and industrywide experience, the business of the Company would be materially enhanced. The convention trip was not intended as compensation nor as a prize or award to Petitioners. Petitioners were compelled by the Company to attend the convention and participate in its activities, to reside in pre-selected hotel accommodations, and to travel (en masse with other agents and officers of the Company) in special trains. What was their undeniable accession to wealth over which they had dominion and control? Suppose Petitioners did not like train travel, New York or conventions. Would this affect the measure of their alleged income? The implausibility of evaluating degrees of pleasure incident to an

employer's business demands (and an employee's response thereto) isolates the error in treating the payment of the convention expenses as constructive income to Petitioners.

II.

If the Petitioners are not charged with gross income in this case, then the alternative argument of business expense is never reached, since the dollars claimed as a deduction obviously must first have been through the tax mill. On the other hand, if the expenditures made by the Company on behalf of Petitioners are included in their gross income, they should be allowed an ordinary and necessary business expense deduction for an equivalent amount. The statute provides that all ordinary and necessary traveling expenses (including the entire amount expended for meals and lodging) while away from home in pursuit of a trade or business are deductible, and it is well-established that the cost of attending a professional or business convention falls within that category. In other words, it is thought to be both "ordinary" and "necessary" in business to attend conventions and to incur expenses in connection therewith. Petitioner, Rudolph, was engaged in the business of being an insurance agent, and he and his wife were away from home attending a convention of his employer's agents when the expenses in question were incurred.

Therefore, the ultimate inquiry is whether the dominant motive and purpose of Petitioners in attending the convention was one of business or pleasure. Were they in pursuit of Rudolph's business or only their own personal whims? In seeking the answer to this inquiry the business purpose of the Company, the industrywide experience, the subtle demands upon Petitioners, and the psychology of business practices all are pertinent and must be examined, for the subjective choice of Petitioners to attend was made in response to these external circumstances and pressures. It is the reason why Petitioners attended, not whether they enjoyed themselves, which is of vital concern.

In this case, Rudolph's agency contract was terminable at will, and he knew that the Company expected him and his wife to attend the convention. Refusal to attend without adequate reason would be tantamount to placing his economic security and his job on the chopping block. His decision to attend and bring his wife was a natural and prudent businessman's response to the demands of his employer. Moreover, the underlying business purpose of the Company was woven deftly into the fabric of the convention, from beginning to end. The group travel arrangements, formal business sessions, choice of speaker, planned entertainment and free time all were designed and intended to instruct, motivate, and encourage the agents and their wives in their business (and the business of the Company). By attending the con-

vention Petitioners participated in an activity which the Company's management, industry experts, and the agents themselves (those best able to judge) believe served a worthwhile business purpose, and to which the Company was willing to devote time, money and effort. Thus, the expenditures attributable to Petitioners were not only necessary, they were unavoidable, since the Company required that they attend the convention and determined the amount spent in their behalf. To assert (as Respondent would do) that Petitioners were away from home for personal reasons and not in pursuit of a business is to make a mockery of the historical reasons for company conventions and to disregard the uncontroverted testimony before the Court.

III.

If the Petitioners are charged with income in this case, the expenditures attribuable to Irma M. Rudolph are ordinary and necessary business expenses for the same reasons that the expenditures attributable to her husband are properly so classified. It is recognized that a wife's expenses on a business trip are deductible if her presence has a bona fide business purpose. What could be more bona fide than if an employer, for its own legitimate business reasons and without intent to compensate, requires that the wife of an employee be present at a convention sponsored by the employer.

ARGUMENT

I.

PETITIONERS DID NOT CONSTRUCTIVELY RECEIVE INCOME WHERE THEY ATTENDED A BUSINESS CONVENTION AT THE BEHEST OF THE COMPANY, THE PAYMENT OF THEIR EXPENSES WAS NOT INTENDED AS COMPENSATION, AND THE CONVENTION WAS ORGANIZED AND EXPECTED TO SERVE THE LEGITIMATE BUSINESS PURPOSES OF INSTRUCTING AND MOTIVATING THE EMPLOYEES OF THE COMPANY.

A. The Concept of a Non-statutory Exception to Gross Income.

Petitioners are cognizant of the broad sweep ascribed by the Court to the term "income" under the tax laws.[1] However, even those decisions which herald the pervasive definition of income in the same breath acknowledge that there may be certain exceptions thereto other than those specifically enumerated in the statute. For instance, in *Comm'r v. Smith, 324 U. S. 177 (1945)*, the Court said:

> "Section 22(a) of the Revenue Act is broad enough to include in taxable income any economic or financial

[1] Eisner v. Macomber, 252 U. S. 189, 64 L. Ed. 521, 40 S. Ct. 189 (1920); Old Colony Trust Co. v. Comm'r, 279 U. S. 716, 73 L. Ed. 918, 49 S. Ct. 499 (1929); Comm'r v. Smith, 324 U. S. 177 (1945); Comm'r v. Glenshaw Glass Co., 348 U. S. 426, 99 L. Ed. 483, 75 S Ct. 473 (1955); James v. United States, 366 U. S. 213, 81 S. Ct. 1052 (1961). Note that Section 22(a) of the Internal Revenue Code of 1939 included as income "gains or profits and income derived from any source whatever." Section 61(a) simplified the statutory language, and eliminated the portion quoted above. However, the amendment was not intended to affect the nature of statutory gross income. Sen. Rep. No. 1622, 83rd Cong., 2d Sess., p. 168. All references hereafter in the text are to the Internal Revenue Code of 1954, unless otherwise specified.

> benefit conferred on the employee *as compensation* (emphasis supplied), whatever the form or mode by which it is effected."

By this language the Court held that any economic or financial benefit conferred on an employee "as compensation" is income, and the form which such compensation may take is immaterial (unless specifically excluded by statute). However, the Court did *not* say that an economic or financial benefit *not* conferred on an employee as compenastion constitutes income.[4] The Court has also said, in *Comm'r v. Glenshaw Glass Co., 348 U. S. 426 (1955)*, that income encompasses

> "• • • undeniable accessions to wealth, clearly realized, and over which the taxpayers have complete dominion."

Stated negatively, if there is no undeniable accession to wealth, if the taxpayer clearly realizes nothing over which he has complete dominion and control, then there may *not* be taxable income. This comports with the Court's view that "income" should be determined on a practical case by case basis.[5]

The conclusion may thus be drawn from these principles that an employee does not realize taxable income when he is the recipient of some benefit (as to which he had no discretion) conferred by his employer without intent to compensate, and the benefit conferred is something essentially subjective and ephemeral, not something which results in an undeniable accession to wealth over which the employee has

[4]The cases do recognize that income need not be earned, *i.e.*, that services need not be rendered. See, *e.g.*, Clarence K. Williams, 35 T. C. , No. 74 (1961). These decisions must be read in the light of others placing an outer limit on the scope of gross income.

[5]See General American Investors Co., Inc. v. Comm'r, 211 F. 2d 522 (2d Cir. 1954), *aff'd*, 348 U. S. 434, 99 L. Ed. 504, 75 S. Ct. 478 (1955).

complete dominion. In other words, the statute does not purport to tax, and the term "income" does not include, what may be called psychic income or the perquisites* of employment. This is in accord with the need for a workable system of producing revenue which does not indulge in the refinements of economists and lexicographers.† The problem is aptly described in *Simons, Personal Income Taxation 53 (U. Chicago Press 1938)*:

> "A similar difficulty arises with reference to receipts in the form of compensation in kind. Let us consider here another of Kleinwachter's conundrums. We are asked to measure the relative incomes of an ordinary officer serving with his troops and a *Flugeladjutant* to the sovereign. Both receive the same nominal pay; but the latter receives quarters in the palace, food at the royal table, servants, and horses for sport. He accompanies the prince to theatre and opera, and, in general—lives royally at no expense to himself and is able to save generously from his salary. But suppose, as one possible complication, that the *Flugeladjutant* detests opera and hunting.
>
> "The problem is clearly hopeless. To neglect all compensation in kind is obviously inappropriate. On the other hand, to include the perquisites as a major addition to the salary implies that all income should be measured with regard for the relative pleasurableness of different activities—which would be the negation of measurement. There is hardly more reason for imputing additional income to the *Flugeladjutant* on account of his luxurious wardrobe than for bringing into account the prestige and social distinction of a (German) university professor. Fortunately, however, such difficulties in satisfactory measurement of relative incomes do not bulk large in modern times; and, again, these elements

*Used here to mean "some advantage, privilege, or incidental benefit resulting from one's employment or office."

†Merchant's Loan & Trust Co. v. Smietanka, 255 U. S. 509, 65 L. Ed. 751, 41 S. Ct. 386 (1921).

of unmeasurable psychic income may be presumed to vary in a somewhat continuous manner along the income scale, * * *."

Similarly, Arthur J. Goldberg, then General Counsel of the CIO, said in a speech:[8]

"The line between (compensation and conditions of employment) is, perhaps, not susceptible of precise definition. The reason it is not is because the line is really an institutional and sociological one. It depends very much on what our current conception of the relative responsibilities of employer and employee happen to be. The question is whether the benefit in question is one which we regard as a proper responsibility which employers should supply for employees as a condition of employment wholly apart from the compensation for their work. And the answers to that question vary from time to time. To the extent that benefits are usually or normally provided by employers, even though they may involve a saving to an employee over alternative methods of providing this facility by himself, then, to that extent the provision of such benefits should not be considered as compensation to the employee but as the provision of improved conditions of work."

B. The Concept Recognized in the Law.

The analysis advanced above is borne out by the pertinent decisions, Congressional Committee reports, and the United States Treasury Regulations themselves. Section 119[9] pro-

[8] See Surrey & Warren, Federal Income Taxation Cases and Materials 106 (Foundation Press, Inc. 1955).

[9] Section 119 reads as follows:

"There shall be excluded from gross income of an employee the value of any meals or lodging furnished to him by his employer for the convenience of the employer, but only if—

(1) In the case of meals, the meals are furnished on the business premises of the employer, or

(2) In the case of lodging the employee is required to use such lodging on the business premises of his employer as a condition of his employment.

In determining whether meals or lodging are furnished for the convenience of the employer, the provisions of an employment contract or of a state statute fixing terms of employment shall not be determinative of whether the meals or lodging are intended as compensation."

vides, in effect, that the value of meals or lodging furnished to an employee by an employer for the convenience of the employer are excludable from income if the meals are furnished on the business premises or the lodging is required to be accepted as a condition of employment. Section 119 is a statutory recognition in a limited area of the underlying concept discussed herein, and Petitioners obviously do not contend that they fall within the ambit of its provisions.

However, prior to the enactment of Section 119, the taxability of meals and lodging furnished to employees turned on two points: (1) were the meals and lodging intended as compensation, and if not (2) were they furnished for the convenience of the employer. See Mim. 6472, 1950-1 Cum. Bull. 15. The cases and rulings held that meals and lodging not intended as compensation and meeting the convenience test did not constitute income to the employee. See *2 Mertens, Law of Federal Income Taxation § 11.16.* The judicial conclusions sanctioning an exclusion from gross income in the absence of specific statutory authorization are proper and just. Nor are such conclusions at odds with the fact that there is an element of gain to the employee in that he received sustenance and quarters which he otherwise would have had to supply for himself. He had nothing he could take, appropriate, use and expend according to his own discretion; rather, the ends of the employer's business dominated and controlled, just as in the furnishing of a place to work and in the supplying of tools and machinery to work with. That personal needs or wants of the employee were

satisfied was merely incidental to the dominant business purposes of the employer.[10]

Thus, Section 119 codified the case law, and modified it to the extent of eliminating the fact question of intent to compensate as a determinant where meals and lodging are furnished in kind.[11] But it did not destroy the fundamental rationale of these earlier decisions as precedent in related or analogous areas; indeed, the committee reports and the regulations under Section 119 acknowledge that today cash allowances for meals and lodging are includible in income *only to the extent that such allowances represent compensation.*[12]

Therefore, it cannot be gainsaid that the courts, Congress, and the Treasury have conceded some benefits conferred upon an employee do die beyond the framework of taxable income. Are there others? What about so-called "fringe benefits" such as use of a library, swimming pool or gymnasium, parking facilities, free medical services, discounts on goods or services, airconditioning, executive offices, special instruction or

[10]Arthur Benaglia, 36 B.T.A. 838 (1937) (acq.). The employee has no unfettered command over the thing. Corliss v. Bowers, 281 U. S. 376 (1936).

[11]Boykin v. Comm'r, 260 F. 2d 249 (8th Cir. 1958); Wolfe v. Comm'r, 59-2 USTC 9558 (4th Cir. 1959). Rev. Rul. 59-307, 1959-2 Cum. Bull. 48. *Cf.* Rev. Rul. 60-348, 1960-2 Cum. Bull. 41 (withdrawing an earlier ruling requiring the inclusion in gross income of the value of meals and lodging furnished to families of resident faculty members of a boarding school as well as the value of meals and lodging furnished for any period during which students were not in residence).

[12]Sen. Rep. No. 1622, 83d Cong., 2d Sess., p. 190 (1954), wherein it is stated: "Section 119 applies only to meals or lodging furnished in kind. Therefore, any cash allowances for meals and lodging received by an employee will continue to be includible in gross income to the extent that such allowances constitute compensation."

Reg. § 1.119-1(c)(2) specifies: "Cash allowances for meals or lodging received by an employee are includable in gross income to the extent that such allowances constitute compensation."

training (on or off the employer's premises) for the purpose of enabling the employee to better perform his job responsibilities, and the myriad of other incidental benefits or privileges that go with one particular job or another.[13] Section 3401 (relating to collection of income tax at source) provides that the term "wages" includes "the cash value of all remuneration paid in *any* (emphasis supplied) medium other than cash". Nevertheless, Reg. § 31.3401(a)-1(b)(10) prescribes an exception:[14]

> "Ordinarily, facilities or privileges (such as entertainment, medical services, or so-called 'courtesy' discounts on purchases), furnished or offered by an employer to his employees generally, are not considered as wages subject to withholding if such facilities or privileges are of relatively small value and are offered or furnished by the employer merely as a means of promoting the health, good will, contentment or efficiency of his employees."

These benefits do not and should not constitute income pro rata to the employees generally, or to those employees who

[13]See Life Magazine (September, 1952), under the caption "Life Goes to Houston's Paradise for Office Girls", wherein the following example is offered:

> "Oveta Smith is an 18-year-old Houston girl, just out of high school, who types and knows some shorthand. In the competitive world of local business, where booming oil companies set the wage scales, she was offered $180 a month by a maritime insurance firm for a clerical job. She turned it down because she prefers making $140 in her present job with the Prudential Life Insurance Company. Her reasons are illustrated on these pages. When Prudential built its new skyscraper it decided to fight the problem of labor turnover without raising its conservative wage level. The Company piled on 'fringe' benefits—not only the usual life insurance and medical checkups, but such unprecedented luxuries as a free swimming pool, free books, free lunches, free tennis courts—in surroundings suggestive of spacious and graceful living. As in the case of Oveta, the system has worked well. So well, in fact, that the vice-president who dreamed up the scheme recently was able to boast that the company didn't have a clerical job open in Houston."

[14]See also Reg. 106, § 402.227; Reg. 107, § 403.227.

avail themselves of one or more. The value thereof is essentially subjective and incapable of measurement, the employees lack discretion or control over their selection, and the underlying objective of the employer is not to compensate the employee but to further the business of the employer. At one end of the spectrum is that which is intended as compensation (in whatever form paid) and therefore represents taxable income; at the other end of the spectrum is that which is a gift as defined by the Court[15] and therefore is nontaxable. Clearly, these fringe benefits would not satisfy the "detached and disinterested generosity" required of a gift, and yet they are nontaxable. They fall somewhere between compensation and gift; somewhere in that nontaxable "twilight zone" which has never been precisely articulated but which is present in all of the decisions and the law.

C. The Concept Applied to the Facts.

Hence we come to the point of applying these principles to the facts before the Court. The District Court held, and the Court of Appeals affirmed, that the convention trip was in the nature of a bonus or compensation, despite uncontroverted testimony to the contrary by the Company's officers and by an independent expert in the field. There was ample evidence before the courts that the Company's decision to hold the convention was based upon sound business objectives, long substantiated by Company and industrywide experience,[16] to

[15]Comm'r v. Duberstein, 363 U. S. 278, 80 S. Ct. 1190 (1960).

[16]Conventions of life insurance agents have been prevalent since 1924. See Report No. 15, Life Insurance Sales Research Bureau (November 1924), Appendix B, p. 57. It is intriguing to note that attribution of income to the agents appears never to have been raised by the Internal Revenue Service despite the elapse of forty years of revenue administration.

instruct and motivate its agents, build esprit de corps, enhance the "family" image of the Company, create interest in sales promotion, and in general further the business of the Company and the agents. The time, effort and planning involved in an undertaking of this sort belie a mere intent to compensate or pay a bonus; the reasons for insurance company conventions are found in much more complex considerations: the nature of an agents' job; energetic competition in the industry; modern business psychology, and other valid business reasons. Respondent would make much of the fact that the agents invited were selected on the basis of production, but this was nothing more than an intelligent and practical method for choosing the agents who would most benefit by the convention.[17] Every sizeable business organization must have some criterion by which to judge the work of its employees and by which to determine those upon whom special training and motivation will be focused. Business does not operate like a school for exceptional children where special attention is devoted to the ones displaying the least aptitude. Obviously, success is recognized. But the convention is not, and was not intended, as a quid pro quo for production.

[17] "What type of person are you going to invite to your conference? Can you draw up a specification of the sort of person you believe will contribute the most"

"What you want is a group of experienced people with keen minds, who are determined to find out all they can about the problem and contribute on the basis of that knowledge to its solution." The Royal Bank of Canada Monthly Letter, Vol. 39, No. 2, page 1 (February 1958), Appendix B, p. 57.

Kenneth B. Skinner, Vice President and Agency Director of the Company, testified (R. 61):

> "Yes, we select the men to attend a convention based upon their proven abilities as well as men showing an aptitude for the business. The amount of business they have written in the past is an important yardstick in our judgment of measuring whether or not they are doing a good job and will continue to do one."

The Court recently had occasion to reiterate the importance of looking to the intent of the payor or transferor in determining the taxability of the recipient. The question in *Commissioner v. Duberstein*, 362 U.S. 278, 80 S. Ct. 1190 (1960), was whether a Cadillac automobile received by a taxpayer from a business associate constituted a gift or taxable compensation. In rejecting the Government's insistence on a new and broad test, the Court said:

> "We take it that the proper criterion, established by decision here, is one that inquires what the basic reason for his conduct was in fact—the dominant reason that explains his action in making the transfer. Further than that we do not think we can profitably go."

The same criterion is applicable here. The dominant reason of the Company in paying the convention expenses of Petitioners is of vital significance, yet the Court of Appeals apparently dismissed this fact without consideration. Unless the uncontradicted testimony before the Court is to be tossed aside as meaningless, a determination must be made as to whether or not the payment of Petitioners' convention expenses constitutes income to them *notwithstanding the absence of any intent to compensate*.

The Court of Appeals ostensibly rests its decision as to the receipt of gross income on the generalization that "receipt by a taxpayer of benefits in a form other than cash may constitute income to him",[15] and on the conclusion that Section 119 is inapplicable. The latter ground for decision may be disregarded, since it is obviously predicated on the mistaken impression that Petitioners claim the coverage of Section 119.

[15] See Patterson v. Thomas, 289 F. 2d 108, 111 (5th Cir. 1961).

On the other hand, the generalization about the receipt of income in kind glosses over the surface and skids to a stop short of the true issue.

As evidenced by the Record, the Petitioners were compelled to go to a company convention; they acted not as a matter of free and independent choice, but in response to the Company's demands. The Company made all arrangements for the convention, and the Petitioners could exercise no discretion in this regard. They were told when to go, what trains to travel on, what hotel and in what room to stay, what to do and when to return. What was their undeniable accession to wealth over which they had dominion and control? Suppose that the Petitioners did not like train travel, New York or conventions.[11] Would the degree of pleasure which they experienced affect the amount of income with which they were charged, and should they be able to recognize a loss if their state of mind was one of actual displeasure? Absurd? Yes. But this is, in essence, the consequence of holding Petitioners to be in receipt of income by virtue of the payment of their convention expenses.

The situation before the Court should be distinguished from a case where an employee is required to travel for his employer, may select his mode of travel, accommodations, etc. and then is reimbursed for his expense on behalf of the employer. The inclusion of the reimbursement in the employee's gross income[12] may be justified on the ground that

[11] C. J. D. Rudolph testified (R. 43): "Whenever I take a trip I like to get away from it all, not have any schedule and do as I please."

[12] Reg. § 1.162-17(b). Note that if expenses are equal to reimbursements, the employee need not report on his tax return reimbursements for travel, transportation, entertainment, and similar purposes paid or incurred by him solely for the benefit of his employer (if he is required to account and does account to his employer for same).

he had sufficient dominion, control and discretion over the conduct of his affairs (*i.e.*, selection of his mode of travel, accommodations, etc.), so that the reimbursement of those costs should be included in the first instance in his gross income, even though he is allowed an offsetting business expense deduction. No such dominion, control or discretion is present here; the only measurement of gain would be the state of mind or psyche of Petitioners, and as, Simons says, this is the negation of measurement.

It is respectfully submitted, therefore, that Petitioners received nothing which constitutes "income" within the meaning of the statute or the Constitution.

II.

IF THE PAYMENT OF EXPENSES ATTRIBUTABLE TO PETITIONERS' TRAVEL TO AND ATTENDANCE AT THE BUSINESS CONVENTION OF THE COMPANY CONSTITUTES TAXABLE INCOME TO PETITIONERS, THEN AN EQUIVALENT AMOUNT IS DEDUCTIBLE BY THEM AS AN ORDINARY AND NECESSARY BUSINESS EXPENSE.

If Petitioners are not required to include in gross income the convention expenses incurred by the Company applicable to them, then their alternative argument is never reached. However, a common thread runs between the argument against constructive attribution of income and the argument in favor of business expense. The same basic facts that lend support to an exclusion from income also, when turned around, confirm the presence of legitimate business expenses; that is, the business purpose of the convention and the neces-

sity for Petitioners to attend in response to the command of the Company.

A. Legislative History of the Statute.

§ Section 63(a), contained in Part I, Subchapter B, Chapter 1, Internal Revenue Code of 1954, specifies that "the term 'taxable income' means gross income, minus the deductions allowed by this chapter * * *." Section 161, contained in Part VI, Subchapter B, of Chapter 1, provides that in computing taxable income under section 63(a) "there shall be allowed as deductions the items specified in this part * * *." Section 162(a) enumerates certain trade or business expenses which fall within the foregoing provisions:

> "There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including—
>
> * * * * *
>
> "(2) traveling expenses (including the entire amount expended for meals and lodging) while away from home in pursuit of a trade or business;"

The predecessor of Section 162 first appeared in Section II, B of the Tariff Act of 1913:

> "That in computing net income for the purpose of the normal tax there shall be allowed as deductions: First, the necessary expenses actually paid in carrying on any business, not including personal, living or family expenses; * * *."

Little or no change was made[21] until the Revenue Act of 1918 which extended the deduction for ordinary and neces-

[21] Clerical changes were made by Section 5(a) of the Revenue Act of 1916, and by Section 1201(1) of the Revenue Act of 1917.

sary expenses in Section 214(a) to those "paid or incurred", and shifted the prohibition against deducting personal, living or family expenses to Section 215(a).[22] The Revenue Act of 1921 added for the first time the language which is now paragraph (2) of section 162(a). The House Report[23] said of the amendment:

> "Section 213 [section 214 of the Senate version] would permit (in the computation of net income) the deduction of all traveling expenses incurred in the pursuit of a trade or business instead of the more limited deduction for such expenses allowed under the present law."

The Senate Report[24] noted that "the deduction for business expenses is *extended* (emphasis supplied) to include all traveling expenses incurred while away from home in pursuit of a trade or business." Thus, it is a fair inference to draw that whatever the law was previously, the Revenue Act of 1921 intended to broaden the deductibility of business expenses, and any construction of the statute should be made in light of this Congressional intent. Although clerical changes have been made,[25] the language of the Revenue Act of 1921 has been carried over into section 162(a)(2).

Congress has not thus far seen fit to restrict the deductibility of travel expenses. In 1959, Senator Clark proposed an amendment[26] to the Tax Rate Extension Act of 1959, which, among other things, would have disallowed deductions for

[22] Now Section 262.

[23] H. R. No. 350, 67th Cong., 1st Sess., p. 11.

[24] Sen. Rep. No. 275, 67th Cong., 1st Sess., p. 14.

[25] The Revenue Act of 1928 consolidated the prior provisions of Section 214(a)(1), relating to individuals, and Section 234(a)(1), relating to corporations, into a single Section 23(a).

[26] S. 2040, to amend H. R. 7523, 86th Cong.

entertainment at public places and travel costs to conventions outside the United States.[27] The amendment was defeated in the Senate Finance Committee. Later, Senator Clark offered an amendment on the Senate floor to accomplish the same basic objectives, and this also was rejected.[28] Two aspects of this legislative proposal are pertinent. First, the restrictions were aimed, in part, at types of activity which might involve pleasure incident to some business purpose, and the rejection of the proposal is significant. Second, the proposal would have disallowed deductions for travel to conventions outside the United States, thereby according left-handed recognition to the legitimacy of travel expenses to conventions inside the United States.

Since 1924 the Treasury regulations[29] under Section 162 and predecessor provisions have stated generally that deductible business expenses include "ordinary and necessary expenditures directly connected with or pertaining to the taxpayer's trade or business", and the Court has amplified this by saying that there must be a "direct and proximate" relationship before the expense is deductible.[30] However, the specific regulation pertaining to travel expenses under

[27] *Query*: The American Bar Association Convention to London, England.

[28] 105 Congressional Record 11897, 11900.

[29] Reg. 65, Art. 101; Reg. 69, Art. 101; Reg. 74, Art. 121; Reg. 77, Art. 121; Reg. 86, Art. 23(a)-1; Reg. 94, Art. 23(a)-1; Reg. 101, Art. 23(a)-1; Reg. 103, § 19.23(a)-1; Reg. 111, § 29.23(a)-1; Reg. 118, § 39.23(a)-1; Reg. § 1.162-1(a).

[30] Kornhauser v. United States, 276 U. S. 145 (1927); Bingham's Trust v. Comm'r, 325 U. S. 365, 65 S. Ct. 1232, (1945). *Cf.* H. R. No. 2333, 77th Cong., 2d Sess., p. 75 (1942), wherein the Ways and Means Committee (discussing the predecessor of Section 212) noted that the "expenses • • • must be ordinary and necessary • • • and must bear a reasonable and proximate relation to the production or collection of income • • •."

section 162(a)(2) has been expanded considerably. Reg. §1.162-2 was adopted by Treasury Decision 6291, approved April 3, 1958, so that the Petitioners are actually governed by the regulation pertaining to the year 1956.[31] Reg. 118, §39.23(a)-2(a), then in force, provided simply:

> "Traveling expenses, as ordinarily understood, include railroad fares and meals and lodging. If the trip is undertaken for other than business purposes, the railroad fares are personal expenses and the meals and lodging are living expenses. If the trip is solely on business, the reasonable and necessary traveling expenses, including railroad fares, meals, and lodging, are business expenses."

However, in disallowing Petitioners a deduction for their convention expense, Respondent ostensibly relies upon an interpretation of the law consistent with the newly-promulgated regulations. Therefore, when considering the application of the regulations to Petitioners, we shall address the discussion to Reg. §1.162-2.

B. Refinement of the Issues.

Any traveling expense to be deductible must be reasonable,[32] and there is no dispute in this case that the expenditures attributable to Petitioners are reasonable. The statute also requires that the expenses be incurred "away from home", and it is apparent that this test is satisfied. Thus, the broad issues are whether Petitioners paid or in-

[31] See Section 7807, for the rules regulating to stop-gap regulations. The specific regulation pertaining to travel expenses first appeared in Reg. 62, Art. 101(a), and the same basic language was carried over into Reg. 118, § 39.23(a)-2(a).

[32] Comm'r v. Flowers, 326 U. S. 465, 90 L. Ed. 203, 66 S. Ct. 465 (1946).

curred "ordinary and necessary"[13] expenses "in the pursuit of a trade or business."

At the outset, it should be noted that an employee is considered to be engaged in a trade or business,[14] and that Rudolph was carrying on the business of being an insurance agent. The question may therefore be restated as follows: did Petitioners attend the convention in pursuit of Rudolph's business as an insurance agent and employee of the Company, and, if so, were their expenses in connection therewith "ordinary and necessary"? "Life in all its fullness must supply the answer to this riddle."[15]

"Ordinary" expenses are not necessarily habitual or normal expenses in the sense that the same taxpayer will have to make them often. *Welch v. Helvering, 290 U.S. 111, 54 S. Ct. 8 (1933); Robinson Land & Lumber Company of Alabama v. United States, 112 F. Supp. 33 (S.D. Ala. 1953); Canton Cotton Mills v. United States, 94 F. Supp. 561 (Ct. Cl. 1951).* The term "ordinary and necessary expense", however, must be given its natural and common connotation. *Tinkoff v. Commissioner, 120 F. 2d 564 (7th Cir. 1941).* An ordinary expense may be one which happens but once in the taxpayer's lifetime if it is a common or frequent occurrence in the type of business in which the expenses are incurred. *Deputy v. DuPont, 308*

[13] Note that the regulations speak of "reasonable and necessary" traveling expenses, but it is not believed that this variation is significant.

[14] See I.T. 4012, 1950-1 Cum. Bull. 33; Rev. Rul. 190, 53-2 Cum. Bull. 302, 305; Rev. Rul. 60-16, 1960-1 Cum. Bull. 58; Noland v. Comm'r, 269 F. 2d 108 (4th Cir. 1959); Reg. § 1.162-2(d). See also 4 Mertens, Law of Federal Income Taxation § 25.08, note call 62.1. Although C.J.D. Rudolph is referred to for convenience as an employee of the Company in the sense that he is employed on a continuing basis as a commissioned agent, his legal status is that of an independent contractor.

[15] Welch v. Helvering, 290 U. S. 111, 54 S. Ct. 8 (1933).

U. S. 488, 60 S. Ct. 363 (1940). The test of a deduction made as an ordinary and necessary expense in carrying on a trade or business is said to be its natural normality and soundness as a business expenditure, in both nature and amount, by general commercial standards, in practical application to the specific situation. *Bryers v. Commissioner, 199 F. 2d 273 (8th Cir. 1952).* Whether an expenditure is both ordinary and necessary will depend upon whether the "average hard-headed businessman" might have made the expenditure.[38] The evidence of customs and actions of organized professional organizations is admissible on the issue of whether certain expenses of a member of that profession at a given time and place are deductible as an ordinary and necessary expense. *Lilly v. Comm'r, 343 U. S. 90, 72 S. Ct. 497 (1952).*

There are many cases which establish that expenses incurred in connection with attendance at professional, business or technical conventions are an "ordinary and necessary" incident of carrying on or pursuing a trade or business, and therefore constitute allowable deductions under section 162 (or its predecessors). Deductions have been allowed to: clergymen attending a church convention;[39] lay member of a church attending a church convention;[40] person attending American Red Cross Convention;[41] lawyer attending tax institute;[42] employee attending convention of related

[38] 4 Mertens, *supra* § 25.09 at 34.

[39] Marion D. Shutter, 2 B.T.A. 23 (1925).

[40] Rev. Rul. 58-240, 1958-1 Cum. Bull. 141.

[41] Henry Carton, 30 T.C. 28 (1958).

[42] Caughlin v. Comm'r, 203 F. 2d 307 (2d Cir. 1953); Bistline v. United States, 145 F. Supp. 802 (D. Idaho 1956). See also Charles O. Gunther, Jr., 1954 P-H T.C. Memo., dec. 54,287.

business group;[41] teachers attending conventions;[42] secretary attending convention of National Secretaries Association;[43] lawyer attending conventions and meetings;[44] university professor attending scientific convention;[45] insurance agent away from home on business;[46] professional cartoonist attending political convention to gather material;[47] physicians attending meetings of medical societies;[48] representatives to annual conventions of trade associations;[49] representatives to the conventions of the United States Chamber of Commerce;[50] furniture store sending its buyers to annual furniture mart;[51] and employees sent to refresher courses to become more acquainted with new processes in the industry.[52]

The instant case is unique and differs from those cited above in that the purpose of the convention was to bring together the scattered employees of a single large business concern rather than independent members of a particular profession or vocation or people having some common but

[41] L. F. Ratterman, 1948 P-H T.C. Memo., Dec. 48,130, *aff'd without opinion*, 177 F. 2d 204 (6th Cir. 1949).

[42] I.T. 3448, 1941-1 Cum. Bull. 206.

[43] Rita N. Callinan, 1953 P-H T.C.M., dec. 53,055.

[44] Wade H. Ellis, 15 B.T.A. 1075, *aff'd*, 50 F. 2d 343 (1929).

[45] Alexander Silverman, 6 B.T.A. 1323 (1927).

[46] Summerour v. Allen, 99 F. Supp. 318 (M.D. Ga. 1951).

[47] J. N. Dowling, 4 B.T.A. 499 (1926).

[48] Wolfe v. McCaughn, 17 AFTR 1007 (E. D. Pa. 1933); Robert C. Doffey, 21 B.T.A. 1242 (1931); Ray Upham, 16 B.T.A. 950 (1929); J. Bentley Squire, 13 B.T.A. 1233 (1928); Cecil M. Jack, 13 B.T.A. 726 (1928).

[49] I.T. 2602, 1931 Cum. Bull. 130.

[50] Letter Ruling signed by C. R. Nash, in reply to a letter dated December 22, 1926.

[51] Finkenburg's Sons, Inc., 17 T.C. 973 (1952).

[52] Pacific Grape Products Company, 17 T.C. 1097 (1952).

otherwise unrelated business interest."[53] This is the first time (together with *Patterson v. Thomas*, *supra*), that such a convention has been subject to analysis by this or any other court with reference to the "ordinary and necessary" requirement for business deductions.[54] However, since 1924 life insurance companies have almost universally sponsored conventions of the type here involved, based upon the business decision that the agents, and thereby the companies, benefit from the knowledge and motivation derived by the agents from the convention.[55]

There is no valid reason to differentiate between the conventions involved in the cited decisions, and a convention of the employees of a single large business concern, such as in the instant case. If the Petitioners attended the convention

---

[53]See Rev. Rul. 59-316, 1959-2 Cum. Bull. 57, which suggests that a taxpayer claiming a deduction for expenses incurred in connection with attending a convention must show that he attended to further his own business. *Cf.* Rev. Rul. 60-16, *supra* note 33, wherein it is indicated that an employee may deduct in computing adjusted gross income the expenses which he incurs in the performance of his services as an employee in attending a business convention.

See also Reg. §1.162-5, which recognizes that an employee's education expenses (including, presumably, travel incidental thereto) in order to meet the express requirement of his employer are deductible:

> "(a) Expenditures made by a taxpayer for his education are deductible if they are for education (including research activities) undertaken primarily for the purpose of:
>
> * * * * *
>
> "(2) Meeting the express requirements of a taxpayer's employer, or the requirements of applicable law or regulations, imposed as a condition to the retention by the taxpayer of his salary, status or employment."

[54]The Commissioner of Internal Revenue recently announced that he acquiesced in the deduction of expenses incurred by individuals in attending conventions of the National Association of Internal Revenue Employees (a convention of employees of a single organization). CCH Fed. Tax Serv., Current Report No. 23, April 19, 1961. The Court of Appeals ascribes some nonbusiness connotation to the fact that the convention was of the employees of a single employer. However, the more logical reaction would be that the converse is true.

[55]See Life Insurance Sales Research Bureau, Report No. 15 (November 1924), Appendix B, p. 57.

for business reasons—that is, if they were in pursuit of a trade or business—their expenses were as "ordinary and necessary" as those of the taxpayers in any of the cited decisions.

C. Petitioners Attended the Convention for Business Reasons.

The ultimate issue, therefore, is the dominant motive and purpose of the Petitioners in attending the convention. Did they attend primarily for reasons of business or personal pleasure? To state the issue is virtually to assume the answer, since both motive and purpose are apparent when an employee acts in deference to the demands of his employer. Nevertheless, the issue must be explored and the facts related to the regulations upon which Respondent depends. Reg. §1.162-2(d) states that:

> "Expenses paid or incurred by a taxpayer in attending a convention or other meeting may constitute an ordinary and necessary business expense under section 162 depending upon the facts and circumstances of each case. No distinction will be made between self-employed persons and employees. The fact that an employee uses vacation or leave time or that his attendance at the convention is voluntary will not necessarily prohibit the allowance of the deduction. The allowance of deductions for such expenses will depend upon whether there is a sufficient relationship between the taxpayer's trade or business and his attendance at the convention or other meeting so that he is benefiting or advancing the interests of his trade or business by such attendance. If the convention is for political, social or other purposes unrelated to the taxpayer's trade or business, the expenses are not deductible."

Note that the test of deduction is made the sufficiency of relationship between the taxpayer's trade or business and his attendance at the convention so that his business is benefitted or advanced by such attendance. In requiring an accomplished benefit or advancement, the regulations probably go beyond anything warranted by the statute. Suppose an employer instructs an employee to attend a convention. *Query:* the relationship between the employee's business (of being an employee) and the convention is demonstrable, but does the negative benefit of not losing his job suffice under the regulations?

The specific regulation pertaining to conventions must be read together with Reg. §1.162-2(b)(1), relating generally to travel expenses:

> "If a taxpayer travels to a destination and while at such destination engages in both business and personal activities, traveling expenses to and from such destination are deductible only if the trip is related primarily to the taxpayer's trade or business. If the trip is primarily personal in nature, the traveling expenses to and from the destination are not deductible even though the taxpayer engages in business activities while at such destination. However, expenses while at the destination which are properly allocable to the taxpayer's trade or business are deductible even though the traveling expenses to and from the destination are not deductible."

This provision permits deduction of travel expenses to and from a destination only if the trip is "related primarily" to the taxpayer's trade or business. It is not known whether this primacy test is the same as the "sufficient relationship" test specified in Reg. §1.162-2(d), and an equally serious

objection may stem from the criterion employed by Reg. §1.162-2(b)(2) for determining whether a trip is related primarily to business or is primarily personal:

> "Whether a trip is related primarily to the taxpayer's trade or business or is primarily personal in nature depends on the facts and circumstances in each case. The amount of time during the period of the trip which is spent on personal activity compared to the amount of time spent on activities directly relating to the taxpayer's trade or business is an important factor in determining whether the trip is primarily personal. If, for example, a taxpayer spends one week while at a destination on activities which are directly related to his trade or business and subsequently spends an additional five weeks for vacation or other personal activities, the trip will be considered primarily personal in nature in the absence of a clear showing to the contrary."

If the trip would not have been undertaken in the first instance were it not for the business reason, the relative times spent at the point of destination on business or personal affairs should be immaterial to the deductibility of expenses of travel to and from such destination.

It cannot be questioned that the formal sessions of the convention bear a direct and proximate relationship to Petitioners' business, since the affairs of the Company and the business of a life insurance agent were the subject matters of those sessions. However, in disallowing a deduction to Petitioners on the ground that the trip was primarily personal Respondent, and both the District Court and the Court of Appeals, stressed the relative times spent in formal session, travel and other activities and the fact that the convention was held in New York.[34] There are two fundamental

errors in the rationale of the lower courts and the theory of the regulations:

First, emphasis upon the relative times spent in planned entertainment, informal activities, and formal business sessions (as if this breakdown was conclusive evidence of an overriding non-business purpose) ignores the historic reason for the convention, the psychological factors in business motivation, the industrywide experience, etc.

Second, regardless of the nature of the activities at the convention (except as they may bear on the question of whether the whole episode was a sham [and in this case, Respondent concedes the bona fides of the convention (R. 67)]), the fact remains that Petitioners were required by the Company to attend and participate. Everything they did in response to the Company's demands, therefore, had a legitimate purpose.

1. *There is no valid basis for distinguishing between travel time and the various activities of the convention as to their business purpose.*

The Court of Appeals asserts that the issue of deductibility must be determined solely from the standpoint of the taxpayers. This is certainly true in the sense that the taxpayers (Petitioners) are the ones claiming the deductions. But the determination cannot be made in a vacuum. This is not a case where the Petitioners embarked on a pleasure jaunt independently of any planned program and at their destination inci-

[58]But *cf.* News Release, IR-394, August 3, 1961, 4 P-H Fed. Tax Serv., par. 32,375, wherein it was stated: "He [the Commissioner] said an analysis of a large group of cases from all parts of the country involving a variety of travel and entertainment expenses did not reveal that any expenses were disallowed merely because of the site of a convention or meeting. * * *."

dentally engaged in business. The Petitioners had no discretion as to the mode and time of transportation, their accommodations or the activities of the convention. Since the Petitioners were the conduit through which the business purpose of the Company was expressed, that same business purpose should be attributed to Petitioners.

For instance, the Petitioners spent almost five full days in enforced and close companionship with other agents and officers of the Company on specially chartered trains, during which time the life insurance business was the principal topic of conversation. This is exactly what the Company expected and intended. It was not mere happenstance that the Company *required* all those attending the convention to travel together. Travel under these circumstances would appear to have greater business substance than unplanned travel alone on some commercial carrier, yet Respondent seeks to disallow the travel expense as being primarily personal.

Likewise, the time spent in informal activity did not detract from the business character of the convention. Although the formal meetings lend continuity to the convention and obviously play an integral part in the instruction and motivation of the agents, perhaps the most invaluable lessons are learned through the give and take of casual conversation among agents. When lawyers get together they talk law; when doctors get together they talk medicine; when insurance men get together, particularly under the circumstances here involved, they talk insurance. Every lawyer knows that the principal benefit of attending a Bar Convention is not derived from what formal lectures are scheduled but rather

from the personal relationship among fellow members of the Bar—talk of a new case, an unusual agreement; talk of common problems; talk about economics of the profession. This was part of the stimulus which the Company wanted to provide. This was the very objective which, through balanced programming, the company desired to achieve.[37] From the moment that the agents and officers of the Company, and their respective wives, boarded the train, to the moment that they returned to Dallas, a dominant business purpose was interwoven into all their activities. The exchange of ideas and methods in informal conversation was as much a part of the plan as the formal meetings.

2. *Because Petitioners were compelled by the Company to attend the convention, all their actions (and the expenses incurred in connection therewith) were for a legitimate business purpose directly and proximately related to Rudolph's business.*

It is one thing to characterize a particular activity as being essentially personal or for business when viewed from the standpoint of preconceived contemporary ideas where such activity is undertaken voluntarily by the taxpayer. It is an entirely different matter when the activity in question is undertaken not voluntarily but as a matter of absolute business compulsion. In other words, it is *why* Petitioners attended, not whether their activities were abstractly pleasur-

[37] Entertainment at a convention is based upon the realization that the delegates are human beings and not mere mechanical cogs in the Company's machine. As such it has a place in every convention, regardless of size. See Report No. 15, Life Insurance Sales Research Bureau (November, 1924), Appendix B, p. 57.

able or whether they enjoyed themselves, which is of vital concern."

For example, suppose an employer orders his employee to attend a convention (or to do any number of things which *might* involve some aspect of pleasure to the employee) and to pay his expenses out of his own pocket. The employee has two alternatives: he can comply with the demand of his employer, or he can refuse to comply and risk the loss of his job. If the employee chooses the sensible course and attends the convention, the fact that he enjoyed himself (or, for that matter, did not enjoy himself) is totally irrelevant to the tax consequences of the expenses incurred, *because his reason for going is singularly and directly related to his business.*

Obviously, if the employer and employee got together and cooked up a scheme to convert a personal expense of the employee into a business deduction, the legitimacy of the deduction could and should be questioned. But in the face of an honest and purposeful business decision, it seems undeniable that the expenses of the employee are directly, proximately and inextricably related to his business.

In the instant case, Rudolph's agency contract was terminable at will, and he knew that the Company expected him to

"The Commissioner has said that "his investigators have launched 'no special drive' against expense account deductions claimed by convention-goers," and that an expense deduction won't be thrown out just because a taxpayer attends a convention in a resort area. He said such deductions are legal if the convention-goer sticks mainly to business matters, no matter how pleasant the surroundings. "Nobody's ever questioned whether you're enjoying yourself at a convention," he declared. "I hope the law is never administered on that basis." See Wall Street Journal, September 29, 1961.

attend the convention. Refusal to attend without adequate reason would be tantamount to placing his economic security and association with the Company in jeopardy. The command of the Company need not be proclaimed as an edict for the meaning to penetrate; the ways of modern business are more subtle, but no less effective. Petitioners decision to attend was a natural and prudent businessman's response to the implicit, but very real, coercion of the Company. What more does the law demand? What is the meaning of the terms "ordinary and necessary", if the actions of Petitioners be not so? As Honorable John R. Brown said in dissent—

> "In a real and vital sense the money is spent for business and business reasons only. It is indispensable. What is indispensable is certainly ordinary and necessary."

Certainly what is indispensable to his business is in pursuit of his business. If the management of a successful company believes that is the best way to further its business, and if the agents attend the convention not only because of the implied command but also because their own business is furthered, then the courts should not strike down the decision of management and reasonable business men in order to substitute that of their own—particularly when the decisions to hold and attend conventions have been accepted for thirty years or more by a nationwide industry as a valuable method

of promoting their business, instructing their agents, and assuring better service for policy holders."

It is respectfully submitted, therefore, that Petitioners should be allowed an ordinary and necessary business expense deduction, if they are charged with income in the first instance because of the payment of their convention expenses.

III.

IF THE PETITIONERS ARE CHARGED WITH INCOME IN THIS CASE, THE EXPENDITURES ATTRIBUTABLE TO IRMA M. RUDOLPH, AS WELL AS THOSE ATTRIBUTABLE TO HER HUSBAND, ARE DEDUCTIBLE AS ORDINARY AND NECESSARY BUSINESS EXPENSES.

The convention expenditures attributable to Irma M. Rudolph are ordinary and necessary business expenses for the same reasons that the expenditures attributable to her husband are properly so classified. It is recognized that a wife's expenses on a business trip are deductible if her presence has a bona fide business purpose, see U. S. Treas. Reg. 1.162-2(c) (1954), and this determination must be made in light of all the facts bearing upon her presence. It is evident

[9]The tax treatment accorded the agents is very material to the Company's objective in sponsoring the convention. The Company has concluded, over long years of experience, that its conventions serve an important business purpose, and neither the Company nor the agents consider the conventions to be a vacation. If the agent is to be taxed for the convention expenses allocable to him, he would likely be of the frame of mind to treat the convention as a vacation and rebel against or disregard the regimentation and basic functions so carefully planned by the Company to meet its objectives. In other words, the business purpose of the Company will be seriously impaired by the imposition upon the agents of a tax based upon conclusions of fact contrary to the expressed intent of both the Company and the agents. This would seem an unwarranted erosion of justifiable business prerogative.

from the testimony before the Court (R. 53), that the Company makes a conscientious and sustained effort to bring the agents' wives into the Company family, and to advise them in a practical manner about the ways they may help their husbands. The Company's efforts in this behalf were not casual and offhand, but were deliberate and carefully considered to achieve their purpose. This has been true on an industrywide basis for years antedating the advent of high taxes! The Company expected Rudolph's wife to attend, and this expectation was not taken lightly by him or the other agents.

If an employee's wife attends a business convention under the guise of a business purpose when in reality the trip is personal, her expenses should not be deductible. But where the Company commands that a wife attend, not for the purpose of offering disguised compensation but for its own legitimate business reasons, and the employee acts in response to that command, the wife's expenses are and should be deductible as ordinary and necessary business expenses."[*]

CONCLUSION

The current controversy about expense account abuses and the efforts of the Treasury to eliminate same are common

[*] See Remarks by Joseph E. Tansill, 14 Journal of Taxation 201, 202:
"Expenses of wives of employees paid by the employer, in attending conventions, * * * seem to constitute another area of spotty enforcement when various parts of the country are contrasted with each other. There are variations among agents in the same district, of course, so that complete uniformity does not exist, but in general it appears that the Middle West has been more vigorous than some other areas on the question of the expense account problems, including wives expenses. *Litigation may ultimately be required to settle these questions*, where the wife's presence is a 'command performance' * * * or where the wife does in fact perform an important function. * * * Modern corporate philosophy regards a key employee's wife as an indispensible member of the team, and many a promising career has been blocked because the individual's wife doesn't measure up."

knowledge.[1] But any inclination to lump life insurance conventions indiscriminately in the category of activities which are criticized by the Treasury would appear to be dangerous and misguided. The holding of life insurance conventions long preceded the era of high taxes, and their purpose is rooted in legitimate and sound business decisions, not tax avoidance. It seems unrealistic, in the inception, to visit upon the Petitioners constructive income predicated essentially on an assumed state of mind. It seems an absolute nullification of the "ordinary and necessary" formula in the statute to disallow Petitioners a business expense deduction if income is, in fact, imputed to them. Perhaps the Congress will determine that the statute produces results undesirable from a socio-economic viewpoint or impossible of orderly administration, and should be changed. Nonetheless, under present law the deduction is proper and should be allowed. The judgment of the court below should be reversed.

Respectfully submitted,

FELIX ATWOOD,
RICHARD A. FRELING, of
TURNER, WHITE, ATWOOD,
MEER & FRANCIS,
1900 Mercantile Dallas
Building,
Dallas 1, Texas,
Attorneys for Petitioners.

[1] Caplin, *The Travel and Entertainment Expense Problem*, 39 Taxes 947 (December, 1961).

APPENDIX A

Section 61, IRC of 1954:

"Sec. 61. (a) GENERAL DEFINITION.—Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items:

(1) Compensation for services, including fees, commissions, and similar items;

(2) Gross income derived from business;

(3) Gains derived from dealings in property;

(4) Interest;

(5) Rents;

(6) Royalties;

(7) Dividends;

(8) Alimony and separate maintenance payments;

(9) Annuities;

(10) Income from life insurance and endowment contracts;

(11) Pensions;

(12) Income from discharge of indebtedness;

(13) Distributive share of partnership gross income;

(14) Income in respect of a decedent; and

(15) Income from an interest in an estate or trust.

(b) CROSS REFERENCES.—

For items specifically included in gross income, see part II (sec. 71 and following). For items specifically excluded from gross income, see part III (sec. 101 and following)."

Section 62, IRC of 1954:

"Sec. 62. For purposes of this subtitle, the term "adjusted gross income" means, in the case of an individual, gross income minus the following deductions:

(1) TRADE AND BUSINESS DEDUCTIONS.—The deductions allowed by this chapter (other than by part VII of this subchapter) which are attributable to a trade or business carried on by the taxpayer, if such trade or business does not consist of the performance of services by the taxpayer as an employee.

(2) TRADE AND BUSINESS DEDUCTIONS OF EMPLOYEES.—

(A) REIMBURSED EXPENSES.—The deductions allowed by part VI (sec. 161 and following) which consist of expenses paid or incurred by the taxpayer, in connection with the performance by him of services as an employee, under a reimbursement or other expense allowance arrangement with his employer.

(B) EXPENSES FOR TRAVEL AWAY FROM HOME.—The deductions allowed by part VI (sec. 161 and following) which consists of expenses of travel, meals, and lodging while away from home, paid or incurred by the taxpayer in connection with the performance by him of services as an employee.

(C) TRANSPORTATION EXPENSES.—The deductions allowed by part VI (sec. 161 and following) which consist of expenses of transportation paid or incurred by the taxpayer in connection with the performance by him of service as an employee.

(D) OUTSIDE SALESMEN.—The deductions allowed by part VI (sec. 161 and following) which

are attributable to a trade or business carried on by the taxpayer, if such trade or business consists of the performance of services by the taxpayer as an employee and if such trade or business is to solicit, away from the employer's place of business, business for the employer."

Section 63(a), IRC of 1954:

"Sec. 63. (a) GENERAL RULING.—Except as provided in subsection (b), for purposes of this subtitle the term 'taxable income' means gross income, minus the deductions allowed by this chapter, other than the standard deduction allowed by Part IV (sec. 141 and following)."

Section 161, IRC of 1954:

"Sec. 161. In computing taxable income under Section 63(a), there shall be allowed as deductions the items specified in this part, subject to the exceptions provided in Part IX (sec. 261 and following, relating to items not deductible)."

Section 162(a), IRC of 1954:

"Sec. 162. (a) IN GENERAL.—There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including—

(1) a reasonable allowance for salaries or other compensation for personal services actually rendered;

(2) traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business; and

(3) rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity.

For purposes of the preceding sentence, the place of residence of a Member of Congress (including any Delegate and Resident Commissioner) within the State, congressional district, Territory, or possession which he represents in Congress shall be considered his home, but amounts expended by such Members within each taxable year for living expenses shall not be deductible for income tax purposes in excess of $3,000."

Reg. §1.162-1(a):

"(a) In general. Business expenses deductible from gross income include the ordinary and necessary expenditures directly connected with or pertaining to the taxpayer's trade or business, except items which are used as a basis for a deduction or a credit under provisions of law other than section 162. The cost of goods purchased for resale, with proper adjustment for opening and closing inventories, is deducted from gross sales in computing gross income. See § 1.61-3(a). Among the items included in business expenses are management expenses, commissions (but see section 263 and the regulations thereunder), labor, supplies, incidental repairs, operating expenses of automobiles used in the trade or business, traveling expenses while away from home solely in the pursuit of a trade or business (see § 1.62-2), advertising and other selling expenses, together with insurance premiums

against fire, storm, theft, accident, or other similar losses in the case of a business, and rental for the use of business property. No such items shall be included in business expenses, however, to the extent that it is used by the taxpayer in computing the cost of property included in its inventory or used in determining the gain or loss basis of its plant, equipment, or other property. Penalty payments with respect to Federal taxes, whether on account of negligence, delinquency, or fraud, are not deductible from gross income. The full amount of the allowable deduction for ordinary and necessary expenses in carrying on a business is nevertheless deductible even though such expenses exceed the gross income derived during the taxable year from such business. In the case of any sports program to which section 114 (relating to sport programs conducted for the American National Red Cross) applies, expenses described in section 114(a)(2) shall be allowable as deductions under section 162(a) only to the extent that such expenses exceed the amount excluded from gross income under section 114(a)."

Reg., § 1.162-2:

"§ 1.162-2. Traveling expenses.—(a) Traveling expenses include travel fares, meals and lodging, and expenses incident to travel such as expenses for sample rooms, telephone and telegraph, public stenographers, etc. Only such traveling expenses as are reasonable and necessary in the conduct of the taxpayer's business and directly attributable to it may be deducted. If the trip is undertaken for other than business purposes, the travel fares and expenses incidental to travel

are personal expenses and the meals and lodging are living expenses. If the trip is solely on business, the reasonable and necessary traveling expenses, including travel fares, meals and lodging, and expenses incidental to travel are business expenses. For the allowance of traveling expenses as deductions in determining adjusted gross income, see section 62(2)(B) and the regulations thereunder.

"(b)(1). If a taxpayer travels to a destination and while at such destination engages in both business and personal activities, traveling expenses to and from such destination are deductible only if the trip is related primarily to the taxpayer's trade or business. If the trip is primarily personal in nature, the traveling expenses to and from the destination are not deductible even though the taxpayer engages in business activities while at such destination. However, expenses while at the destination which are properly allocable to the taxpayer's trade or business are deductible even though the traveling expenses to and from the destination are not deductible.

"(2). Whether a trip is related primarily to the taxpayer's trade or business or is primarily personal in nature depends on the facts and circumstances in each case. The amount of time during the period of the trip which is spent on personal activity compared to the amount of time spent on activities directly relating to the taxpayer's trade or business is an important factor in determining whether the trip is primarily personal. If, for example, a taxpayer spends one week while at a destination on activities which are directly related to his trade or business and subsequently spends an additional five

weeks for vacation or other personal activities, the trip will be considered primarily personal in nature in the absence of clear showing to the contrary.

"(c). Where a taxpayer's wife accompanies him on a business trip, expenses attributable to her travel are not deductible unless it can be adequately shown that the wife's presence on the trip has a bona fide business purpose. The wife's performance of some incidental service does not cause her expenses to qualify as deductible business expenses. The same rules apply to any other members of the taxpayer's family who accompany him on such a trip.

"(d). Expenses paid or incurred by a taxpayer in attending a convention or other meeting may constitute an ordinary and necessary business expense under section 162 depending upon the facts and circumstances of each case. No distinction will be made between self-employed persons and employees. The fact that an employee uses vacation or leave time or that his attendance at the convention is voluntary will not necessarily prohibit the allowance of the deduction. The allowance of deductions for such expenses will depend upon whether there is a sufficient relationship between the taxpayer's trade or business and his attendance at the convention or other meeting so that he is benefiting or advancing the interests of his trade or business by such attendance. If the convention is for political, social or other purposes unrelated to the taxpayer's trade or business, the expenses are not deductible.

"(e). Commuters' fares are not considered as business expenses and are not deductible.

"(f). For rules with respect to the reporting and substantiation of traveling and other business expenses of employees for taxable years beginning after December 31, 1957, see §1.162-17."

Reg. § 39.23(a)-2:

"(a) Traveling expenses, as ordinarily understood, include railroad fares and meals and lodging. If the trip is undertaken for other than business purposes, the railroad fares are personal expenses and the meals and lodging are living expenses. If the trip is solely on business, the reasonable and necessary traveling expenses, including railroad fares, meals and lodging, are business expenses.

"(b) If, then, an individual, whose business requires him to travel, receives a salary as full compensation for his services, without reimbursement for traveling expenses, or is employed on a commission basis with no expense allowance, his traveling expenses, including the entire amount expended for meals and lodging, are deductible from gross income.

"(c) If an individual receives a salary and is also paid his actual traveling expenses, he shall include in gross income the amount so repaid and may deduct such expenses.

"(d) If an individual receives a salary and also an allowance for meals and lodging, as, for example, a per diem allowance in lieu of subsistence, the amount of the allowance should be included in gross income and the cost of such meals and lodging may be deducted therefrom.

"(e) A payment for the use of a sample room at a hotel for the display of goods is a business expense.

"(f) Only such expenses as are reasonable and necessary in the conduct of the business and directly attributable to it may be deducted.

"(g) A taxpayer claiming the benefit of the deductions referred to in this section must attach to his return a statement showing (1) the nature of the business in which engaged; (2) the number of days away from home during the taxable year on account of business; (3) the total amount of expenses incident to meals and lodging while absent from home on business during the taxable year; and (4) the total amount of other expenses incident to travel and claimed as a deduction.

"(h) Claim for the deductions referred to in this section must be substantiated, when required by the Commissioner, by evidence showing in detail the amount and nature of the expenses incurred.

"(i) Commuters' fares are not considered as business expenses and are not deductible."

APPENDIX B

Royal Bank of Canada Monthly Letter, Vol. 39, No. 2, page 1 (February, 1958):

"Conferences of all sizes and sorts are important in business life, in professional life, in politics and in the home. Many a person has been frustrated in carrying out his plans because he did not consult the people concerned, learn their ideas, and win their interest.

"The conference we are about to plan is not a convention of men and women who have come together for good cheer, but a meeting of people to discuss issues of interest to them, to contribute ideas, and to carry away thoughts that will be worth remembering.

"We live in a society of growing complexity, in which no one person can know all about anything. A conference brings together people with diverse notions and varied kinds of information. The exchange of thoughts and the pooling of ideas and the study of solutions—these are the essence of the conference method.

"There are subsidiary benefits, too. A conference will give the people who participate in it a better sense of identity. They will be confirmed in their partnership in a common effort. They will prove to themselves the benefit of convincing and persuading rather than overruling one another.

• • • • •

"Do not lose sight of the splendid opportunity this gathering gives you to tap the creative resources of all these individuals who come to your conference inspired by fellowship in a mutual endeavor and stimulated by the exchange of ideas. Determine at the beginning to so shape your conference as to make the most of it. If people go away from your conference with the feeling of belonging to your organization in a valuable way, that is a bonus value that may be more important to your business than all the other conference benefits.

"This statement is true of all sorts of conferences, from the great trade association conference through those of individual businesses and professional societies, to the family conference. * * *."

* * * * *

"What type of person are you going to invite to your conference? Can you draw up a specification of the sort of person you believe will contribute most?

"What you want is a group of experienced people with keen minds, who are determined to find out all they can about the problem and contribute on the basis of that knowledge to its solution."

Report No. 15, Life Insurance Sales Research Bureau (November, 1924) (Excerpts from same):

"One of the chief things to be accomplished by a convention is to secure unanimous understanding of the principles underlying the company's sales operations and the rules which experience has proved to be essential in carrying out those principles. There is no sales organization anywhere which ha. a complete and unanimous grasp of these matters but a convention can do more to give the men that grasp than anything else. Home Offices are constantly under the necessity of formulating principles and rules, and they are similarly in a constant state of disappointment because they are not understood. The convention is the place above all others where this can be accomplished."

* * * * *

"The extent to which the Home Office arranges for transportation depends largely upon the situation of the convention city. If it is centrally located with many lines of approach, it would be impracticable to arrange for many men to meet on their way to the convention. But if the convention is to be held in an isolated spot, or one at considerable distance from the home of the majority of the members attending, then specific plans may be made for assembling at some nearer location

and proceeding together to the destination. If this latter is at all feasible, it is desirable for several reasons. It gives the men a peculiar feeling of satisfaction to travel on a "special" train or on "special" cars, it encourages a friendlier feeling than is generally present at conventions at which the men arrive as strangers, it makes the men more anxious to get down to the real work of the convention when they arrive at their destination, and, above all, it has a decided educational value in its contacts and ever present business discussions."

• • • • •

"Today an ever increasing number of wives take a real interest in what their husbands do, and this interest is frequently referred to by men as being of very great value to them. In fact, it has been said that a wife can not usually be so wholly lacking in contact with her husband's work as to have no influence at all upon it.

"In many cases, this influence is negative rather than positive, and this is particularly true in the careers of many life insurance agents because their work frequently involves evening appointments—a condition usually resented by a wife. Many a wife has thoroughly discouraged her husband because the only thing which she ever knew about his work was that he had to go out at night or that he had failed to 'write that ten' which would give her a new dress. She knew nothing about the bigger things which life insurance accomplishes and of which her husband was or could be a part. The recognition of the very great desirability of 'selling' the wife on her husband's job has spread rapidly in recent years, and today many husbands are helped over the rough spots of their career by the enthusiasm and vision of their wives, much of which can be aroused or increased at a convention."

• • • • •

"Whether a convention is intended to provide instruction or to arouse company loyalty through inspirational talks, there is one thing which should run through all

its preliminary plans and all its sessions, the spirit of cordiality and hospitality. As one company expressed it —'We always try to do just a little bit more for our men than they expect."

"The public expects much of the life insurance business in the way of intelligent, prompt service, and this service is made up of that which is contributed by the Home Office as well as by the agent. The Home Office continually strives to improve both of these factors, and one of its best opportunities to show to its field force the kind of service which it is capable of rendering is at its convention.

"We have endeavored to describe in the preceding pages those items which appear to contribute to the smooth running of a meeting, but over and beyond such matters are the almost countless things which can be done for the pleasure of the visitors. From the moment when they first hear of the proposed meeting until they have returned to their desks, the company has innumerable, small opportunities to impress them with the fact that their company is far from a 'soulless corporation'. It is these human relations which steady and even inspire many a man in days of doubt and discouragement, in those days when he thinks that perhaps he is in the wrong business or in the wrong company."